Decision **DRAFT DECISION OF ALJ THOMAS (Mailed 10/4/2004)**

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

In the matter of the Application of SIERRA PACIFIC POWER COMPANY for an Order Authorizing the Sale of Four Hydroelectric Generation Plants on the Truckee River to the Truckee Meadows Water Authority.	Application 03-09-045 Filed September 30, 2003)

O P I N I O N

I. Summary

This decision grants Sierra Pacific Power Company's (Sierra) application pursuant to Pub. Util. Code § 851 to sell its four run-of-the-river hydroelectric generating plants on the Truckee River to the Truckee Meadows Water Authority (TMWA). The sale of these electric generating plants is authorized by statute, and is in the public interest. Further, there will be no adverse environmental impact as a result of the sale.

However, Sierra has not provided adequate explanation of its proposed gain on sale allocation. Because of our recent initiation of Rulemaking (R.) 04-09-003, examining how to allocate gains from the sale of utility property, the issue should be addressed once that Rulemaking is resolved.

II. Background

Sierra owns four run-of-the-river hydroelectric generating plants[1] at Farad, California and Fleish, Verdi and Washoe, Nevada. Sierra is an investor-owned public utility that provides retail electric service to customers in northern Nevada and portions of eastern California. Sierra serves approximately 44,000 customers in California, most of whom are located in and around the Lake Tahoe Basin.

On January 15, 2001, Sierra Pacific agreed to sell its retail water business, including the plants, to the TMWA, conditioned upon Commission approval of the sale. The purchase price is $8 million. The Asset Purchase Agreement (APA) between the two entities is the product of a long series of negotiations involving Sierra, the TMWA and many other entities, and is designed to ensure adequate water supply and fish spawning grounds, among other things, in the Lake Tahoe and Truckee River areas.[2]

The approval Sierra seeks here is but one in a long list of approvals required to complete a full reorganization of water rights and obligations in

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[1] A run-of-the-river plant has no reservoir storage. It generates electricity only when there is adequate water flow in river on which it is located.

[2] *See, e.g., Truckee River Operating Agreement*, Federal Register: April 15, 2004 (Volume 69, Number 73) (U.S. Department of the Interior notice of intent to prepare draft environmental impact statement/environmental impact report for the Draft Truckee River Operating Agreement (TROA) which would implement Section 205(a) of the Truckee-Carson-Pyramid Lake Water Rights Settlement Act of 1990, Title II of Pub. L. 101-618 (Settlement Act)), available on the Internet at http://www.epa.gov/fedrgstr/EPA-IMPACT/2004/April/Day-15/i8570.htm.

foregoing areas. These rights and obligations appear in full in the TROA,[3] a document applicable to, among others, the United States, California, Nevada, Sierra, the Pyramid Lake Paiute Tribe, the Washoe County Conservation District, and the Cities of Reno and Sparks, Nevada.

The TMWA is a publicly-owned municipal water utility that provides retail commercial and residential water services to customers in portions of the cities of Reno and Sparks, Nevada.[4]

Sierra proposes to transfer the water rights associated with its right to divert water from the Truckee River for hydroelectric generation to TMWA. Those water rights were established under the Orr Ditch Decree, Claims 4 through 9,[5] allowing Sierra to divert water from the Truckee River to produce electricity in its run-of-the-river generating plants.

In Decision (D.) 03-04-043,[6] this Commission found that an earlier application Sierra filed was not sufficient to allow the Commission to address the request and analyze its environmental impacts. We denied the application

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[3] A current copy of the TROA is available on the Internet at http://www.usbr.gov/mp/lbao/troa.

[4] The TMWA was established pursuant to a Cooperative Agreement among the City of Reno, the City of Sparks, and Washoe County to establish a Joint Powers Authority (Authority) pursuant to the Nevada Interlocal Cooperation Act (NRS Chapter 277.080 through 277.180) for the purpose of acquiring Sierra's water business assets. *See* Op. Nev. Att'y Gen. No. 2000-34 (Dec. 2000), *cited in* Public Utilities Commission of Nevada's May 4, 2001 Order in its Docket 01-1044, available on the Internet at http://www.puc.state.nv.us/water/dkt_01-1044/01-1044o2.pdf.

[5] *United States v. Orr Water Ditch Co.*, Equity No. A–3 (D. Nev. 1944), *cited in United States v. Nevada*, 415 U.S. 534 (1973). Sierra describes this litigation and the resulting decree at length in Chapter 4 of the testimony accompanying its application.

[6] 2003 Cal. PUC LEXIS 270.

without prejudice, and granted Sierra the right to file a new application, with adequate justification, including a proponent's environmental assessment (PEA). Sierra filed this application, accompanied by the required PEA, on September 30, 2003.[7]

Utilities may not generally sell their electric generating plants.[8] However, on September 24, 2002, Assembly Bill 1235 was signed into law, amending Pub. Util. Code § 377 to allow Sierra to sell these four plants. Section 377.1 states that § 377, barring generally the sale of generating plants, "does not apply to the four run-of-river hydroelectric project works located on the Truckee River. . . ." Section 377.1 became effective on September 24, 2002.

Each plant, when running at full capacity, produces roughly 2.5 megawatts (MW) of electricity. However, Sierra states that only 5.6 percent of its total electric generation serves California, and that these run-of-the-river plants operate at full capacity only a few months during the year when water levels in the Truckee River permit diversions for hydroelectric generation. Thus, according to Sierra, at maximum capacity, the 10 MW associated with these plants will reduce the power available to California customers only by 0.56 MW. At actual capacity – 4.7 MW for the 12 months ended September 2002 – only 0.26 MW was allocated to California. Sierra thus asserts that the electricity loss to California would be *de minimis.* Moreover, since Sierra believes that TMWA will

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[7] Application (A.) 02-12-007, filed December 5, 2002.

[8] Cal. Pub. Util. Code § 377 ("[N]o facility for the generation of electricity owned by a public utility may be disposed of prior to January 1, 2006.") We have interpreted Section 377 to bar other generating plant sales. *See, e.g.,* D.04-05-019, 2004 Cal. PUC LEXIS 225.

continue to operate the hydroelectric generation portion of the plants' output, Sierra asserts that even this small reduction in electric capacity may not come to pass.

No party has protested the application.

III. Discussion

We have four tasks in evaluating Sierra's application. First, we must determine whether the sale is lawful given the general ban on sale by utilities of electric generation assets. Second, we must evaluate whether the sale is in the public interest pursuant to Pub. Util. Code § 851. Third, we must determine whether the project will have an adverse environmental impact. Finally, we must determine whether Sierra's proposed ratemaking treatment for the sale proceeds is appropriate. We analyze each issue below.

A. May Sierra Sell Generation Assets?

There is no controversy over Sierra's ability to sell the plants, since there is a statute specifically exempting the four plants at issue from the general Pub. Util. Code § 377 ban on utility sale of generation assets. Thus, Sierra may legally sell the Farad, Verdi, Fleish and Washoe plants pursuant to Pub. Util. Code § 377.1.

B. Is the Sale in the Public Interest?

Sierra seeks an exemption from the requirements of § 851 "based on the fact that the transfer of the hydroelectric plants is in the public interest."[9] As we found in D.03-02-022,[10] involving the sale of the other plant subject to § 377.1,

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[9] Application, vol. I, at 2.

[10] 2003 Cal. PUC LEXIS 112, at *2.

§ 851 applies to this case, so an exemption is not appropriate. Sierra's sale must satisfy the requirements of § 851 in order to be approved.

Section 851 states in part that no public utility "shall sell, lease, . . . or otherwise dispose of or encumber the whole or any part of . . . property necessary or useful in the performance of its duties to the public, . . . without first having secured from the Commission an order authorizing it to do so." As an integral part of the Commission's decision-making process in reviewing a § 851 application the Commission may "take such action, as a condition to the transfer, as the public interest may require."

In D.03-02-022, we found that prior to allowing a sale of electric generating plants, we must find that "the . . . facility[y] is no longer used and useful as defined in § 851."[11] In that case, we found this criterion was met: "The prepared testimony in this proceeding shows that the . . . facility is not critical to system reliability. This is an old plant, its output is small and it is run-of-the-river, which means that it can only generate power when there is sufficient water flow."[12]

Here, Sierra claims the sale is in the public interest for two reasons. First, it states that it has sufficient resources to continue serving the electricity needs of its California customers without the output from the four plants, which all date from the turn of the 20th century. Indeed, according to Sierra, since the plants "presumably will continue operation," there will be no impact of the sale of the

[11] *Id.* at *3.

[12] *Id.* at *4.

plants on system reliability.[13] However, Sierra's testimony also states that, "entry into effect [sic] of the TROA will reduce the amount of power generated by these hydroelectric facilities."[14]

Nonetheless, we have no evidence to counter Sierra Pacific's assertion that it will retain sufficient electric capacity to serve the needs of its customers. Further, we agree with Sierra that the electricity the four run-of-the-river plants generate is *de minimis* and that loss or diminution of this output will not have an adverse impact on Sierra's ability to serve the public. Thus, this factor militates in favor of granting the application.

Second, Sierra asserts that the sale is part of a much larger, and essential, reorganization of the water resources in the Lake Tahoe and Truckee River areas that ultimately will preserve the resources while protecting the rights of all involved:

> Sierra believes that the public interest is necessitated [sic] by the operational interrelationship of the water rights for municipal supply and the water rights for hydroelectric generation as well as the need to settle all outstanding issues between the United States, the Pyramid Lake Tribe, California, Nevada and the purveyor of water in the Truckee Meadows relating to the operation of the Truckee River reservoirs known at [sic] the Negotiated Settlement and the Truckee River Operating Agreement (TROA). . . .[15]

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[13] Nothing in this decision should be construed to grant authority to TWMA to offer water or electric service in California.

[14] Application, Vol. II, ch. 4, at 16.

[15] Application, vol. I, at 2-3.

We do not have an adequate record before us to determine whether the sale Sierra proposes is integral to the TROA, or whether the TROA itself is in the public interest. Sierra cites many obstacles to ultimate adoption of the TROA in its testimony. In our view, we are not equipped to determine whether overall resolution of water disputes in the Tahoe and Truckee River areas, as embodied in the TROA, is in the public interest or supports granting this application.

Thus, we have one ground on which to grant this application – the evidence that the sale will not impair Sierra's ability to provide electricity to its customers and therefore that the plants are not critical to system reliability. While the evidence could be stronger, based on the record before us, we find that the sale of the plants is in the public interest and therefore satisfies the requirements of Pub. Util. Code § 851.

We also required in D.03-02-022 that the applicant demonstrate that it had permission from other regulators with jurisdiction over the plants. Here, three of the plants are located in Nevada. According to Sierra, "the Public Utilities Commission of Nevada (PUCN) approved the sale of Sierra's water business assets to TMWA including the hydroelectric plants and associated water rights, on April 27, 2001, in Docket No. [01-1044.]"[16] We have examined the PUCN's April 27, 2001, decision and agree with Sierra that the PUCN has approved the Nevada aspects of this transaction.[17]

Thus, the sale satisfies the requirement of § 851.

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[16] Application, vol. I, at 7.

[17] The PUCN approved the ratemaking aspects of the transaction in a later decision issued on May 4, 2001.

C. Will the Sale Cause Adverse Environmental Impact?

On June 9, 2004, the Commission issued a Notice of Intent to Adopt a Negative Declaration pursuant to the California Environmental Quality Act (CEQA), and invited public comment on the accompanying Initial Study and Negative Declaration (ISND). Under CEQA, the Commission must prepare an Initial Study for discretionary projects such as Sierra's proposed plant sale to determine whether the project may have significant adverse effect on the environment. If the Initial Study does not reveal substantial evidence of such an effect, or if the potential effect can be reduced to a level of insignificance thorough project revisions, the Commission may adopt a Negative Declaration.

No party objected to adoption of the Negative Declaration. On July 19, 2004, the State Office of Planning and Research (OPR), which acts as a clearinghouse for CEQA documents, notified us that the Commission had complied with clearinghouse requirements and that no state agencies submitted comments on the ISND.

Thus, on August 6, 2004, the Commission issued a Final Negative Declaration finding that Sierra's project would have no impacts in the areas CEQA requires be analyzed: aesthetics, agricultural resources, air quality, biological resources, cultural resources, geology and soils, hazards and hazardous materials, hydrology and water quality, land use planning, mineral resources, noise, population and housing, recreation, transportation and traffic, or utilities and service systems.

In accordance with the Final Negative Declaration, we find that sale of the plants will not cause adverse environmental impact.

D. Is Sierra's Ratemaking Treatment Appropriate?

The final issue in this proceeding relates to how Sierra should account for the proceeds from the sale. As noted, the sales price is $8 million. Sierra states that as a result of the sale, Sierra's California customers will receive a decrease in revenue requirement of $12,000, or 0.02%. According to Sierra, this decrease will occur because of the removal of the plants and associated depreciation from rate base; removal of the hydro related expenses; increase in fuel and purchased power costs; and amortization of the gain associated with the sale over three years.

Sierra does not adequately detail its proposed allocation of the gain on sale. We have just opened a Rulemaking to address the appropriate allocation of gains on sale of utility property, R.04-09-003. In light of the new Rulemaking, we defer a decision on this topic until Sierra has properly documented the allocation and we have a resolution in R.04-09-003 of the appropriate treatment of gains on sale.

We will close Sierra's application at this time. Sierra should hold the gain on sale in a memorandum account for the time being. When we issue a decision in R.04-09-003, Sierra shall file an Advice Letter, and serve it on the service list for R.04-09-003, setting forth its proposed allocation in detail, and proposing an allocation consistent with the decision.

IV. Comments on Draft Decision

The draft decision of the Administrative Law Judge (ALJ) in this matter was mailed to the parties in accordance with Pub. Util. Code § 311(g)(1) and Rule 77.7 of the Rules of Practice and Procedure. Sierra filed comments on October 22, 2004. We make changes to the decision to reflect those comments, which do not change the outcome of our decision.

V. Assignment of Proceeding

Susan P. Kennedy is the Assigned Commissioner and Sarah R. Thomas is the assigned Administrative Law Judge in this proceeding.

Findings of Fact

1. The hydroelectric facilities at issue are old and are not needed for system reliability.
2. The CPUC is the Lead Agency for the proposed project under CEQA
3. On June 9, 2004, the CPUC prepared a Draft Negative Declaration for the project, which found that the proposed project would have a less than significant effect on the environment.
4. No party filed comments on the Draft Negative Declaration.
5. On August 6, 2004, the CPUC issued a Final Negative Declaration.
6. The proposed project will not result in adverse environmental impact.
7. Sierra does not adequately detail its proposed allocation of the gain on sale.

Conclusions of Law

1. The sale of the hydroelectric plants is authorized by Pub. Util. Code § 377.1.
2. The sale is in the public interest.
3. The sale is authorized pursuant to § 851.

4. The Final Negative Declaration was prepared and completed in accordance with the requirements of CEQA.

5. Disposition of the gain on sale of the power plants should await a decision in R.04-09-003.

O R D E R

IT IS ORDERED that:

1. Pursuant to Pub. Util. Code § 851, Sierra Pacific Power Company (Sierra) is authorized to enter into the Asset Purchase Agreement attached as Exhibit B to its application with the Truckee Meadows Water Authority (TMWA).

2. This order does not allow TMWA to engage in the provision of water or electricity service in California.

3. Sierra shall place the gain on sale from the power plants in a memorandum account for the time being. Once we issue a decision in Rulemaking (R.) 04-09-003, Sierra shall file an Advice Letter, and serve it on the service list for R.04-09-003, setting forth its proposed allocation in detail, and proposing an allocation consistent with the decision in R.04-09-003.

4. We adopt the Final Negative Declaration.

5. This proceeding is closed.

This order is effective today.

Dated _____, at San Francisco, California.